

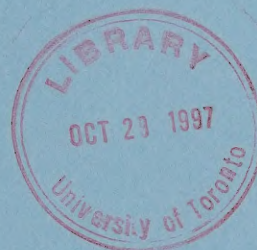


National Energy Board

Reasons for Decision

44
Novagas Canada Ltd.

MH-2-97



October 1997

Taylor Extraction Rights

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National Energy Board

Reasons for Decision

In the Matter of

Novagas Canada Ltd.

Application dated 12 May 1997 requesting that the Board inquire into the practices of Westcoast Energy Inc. with respect to gas stripping arrangements at Taylor, British Columbia.

MH-2-97

October 1997

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Cat. No. NE22-1/1997-12E
ISBN 0-662-26171-2

This report is published separately in both official
languages.

Copies are available on request from:

The Publications Office
National Energy Board
311 Sixth Avenue S.W.
Calgary, Alberta T2P 3H2
E-Mail: orders@neb.gc.ca
Fax: (403) 292-5503
Phone: (403) 292-3562

For pick-up at the NEB office:

Library
Ground Floor

Printed in Canada

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représenté par l'Office national de l'énergie

N° de cat. NE22-1/1997-12F
ISBN 0-662-82389-3

Ce rapport est publié séparément dans les deux
langues officielles.

Exemplaires disponibles sur demande auprès du:

Bureau des publications
Office national de l'énergie
311, sixième avenue s.-o.
Calgary (Alberta) T2P 3H2
C. électr. : orders@neb.gc.ca
Télécopieur : (403) 292-5503
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En personne, au bureau de l'Office:

Bibliothèque
Rez-de-chaussée

Imprimé au Canada

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Abbreviations

Act	National Energy Board Act
B.C.	British Columbia
BCPC	British Columbia Petroleum Corporation
CanWest	CanWest Gas Supply Inc.
GSA	Gas Stripping Agreement
LMA	Liquids Measurement and Allocation
MMcfd	million cubic feet per day
NCL	Novagas Canada Ltd.
NEB or Board	National Energy Board
NGL	Natural Gas Liquids
Petro-Canada	Petro-Canada Limited
Solex	Solex Gas Liquids Ltd.
Westcoast	Westcoast Energy Inc.

Recital and Appearances

IN THE MATTER OF the *National Energy Board Act* (the "Act"), and the Regulations made thereunder; and

IN THE MATTER OF an application dated 12 May 1997 by Novagas Canada Ltd. requesting that the Board inquire into the practices of Westcoast Energy Inc. ("Westcoast") with respect to gas stripping arrangements at Taylor, British Columbia; and

IN THE MATTER OF Hearing Order MH-2-97;

HEARD in Calgary, Alberta on 15, 16, 17, and 29 September 1997.

BEFORE:

A. Côté-Verhaaf	Presiding Member
K.W. Vollman	Member
J.A. Snider	Member

APPEARANCES:

A.S. Hollingworth	Novagas Canada Ltd.;
D.M. Wood	Canadian Natural Resources; and
R.T. Housman	Humble Petroleum Marketing Ltd.
N.J. Schultz	Canadian Association of Petroleum Producers
B. Troicuk	
B.A. Stevenson	Alberta Natural Gas Company Ltd
S.H. Castonguay	Amoco Canada Petroleum Company Ltd.
E.C. Eddy	BC Gas Utility Ltd.
B. Woods	Duke Energy Marketing Limited Partnership
D.A. Holgate	Northwest Pacific Energy Marketing Inc.
D.G. Davies	Solex Gas Liquids Ltd., General Partner; Taylor Gas Liquids Limited Partnership
G.K. Macintosh, Q.C	Westcoast Energy Inc.
B.J. Roth	
S.B. Horne	
P.A. McCunn-Miller	PanCanadian Petroleum Limited
P. Kahler	
C.J.C. Page	Alberta Department of Energy

D. Green

Province of British Columbia, Ministry of Employment and
Investment

C. McKinnon

Board Counsel

Chapter 1

Background and Application

1.1 Background

In 1985, Westcoast Energy Inc. ("Westcoast") entered into a joint venture with Petro-Canada Limited ("Petro-Canada") for the construction of a natural gas liquids ("NGL") plant at Taylor, British Columbia ("B.C.") in order to "deep cut" the residue gas supply delivered from the McMahon Plant; i.e., to recover propane, butane and condensate from the residue gas stream for the purposes of resale. At the time of construction, the Board decided that it would not regulate the NGL plant as the plant was neither a necessary nor an integral part of Westcoast's pipeline system and, therefore, it was not a part of Westcoast's federally-regulated pipeline undertaking.

Under a gas stripping agreement dated 1 May 1986 between Westcoast and Petro-Canada, Westcoast agreed to make available to the NGL plant for liquids extraction all residue gas owned or controlled by Westcoast which was delivered to the outlet of the McMahon Plant. This agreement further required the NGL plant joint venture to redeliver to Westcoast a daily volume of marketable quality pipeline gas which was thermally equivalent to the liquids extracted from the gas stream in the NGL plant. This is referred to as make-up or shrinkage gas. At that time, Westcoast, in addition to being owner and operator of the pipeline, held title to all the natural gas in its system, with the B.C.-sourced gas being purchased pursuant to an arrangement with the British Columbia Petroleum Corporation ("BCPC").

Between 1986 and 1991, Westcoast's pipeline operations evolved from a merchant function to a transportation function. In 1990, the Government of British Columbia privatized the gas marketing business of the BCPC. The BCPC was acquired by CanWest Gas Supply Inc. ("CanWest"), and the BCPC Agreement dated 1 November 1985 was assigned to CanWest.

In 1995, Westcoast and Petro-Canada sold the NGL plant to Solex Energy Company Inc. and Solex Developments Company Inc. and the BCPC Agreement was assigned by Westcoast and Petro-Canada to Solex, with the consent of CanWest. The Taylor Gas Liquids Fund acquired title to the NGL plant in 1996; it is currently being operated by Solex Gas Liquids Ltd. ("Solex").

At the time of the sale of the NGL plant, Westcoast entered into a Gas Stripping Agreement ("GSA") dated 1 May 1995 with Solex, which replaced the earlier gas stripping agreement dated 1 May 1986. The GSA contemplates Westcoast making available to Solex, for the sole purpose of extracting NGL, up to $11.9 \times 10^6 \text{ m}^3/\text{d}$ (420 MMcfd) of residue gas from the McMahon Plant. Under the GSA, Solex delivers make-up gas at the outlet of the Solex Plant to replace the shrinkage resulting from the extraction of the NGL and provides hydrocarbon dew-point and sulphur removal services to Westcoast.

Westcoast reserves pipeline capacity on its main transmission pipeline for make-up gas delivered by Solex to Westcoast, with no toll or charge applicable for the transportation of the make-up gas. The transmission of make-up gas in this manner is an arrangement dating back to the inception of the NGL plant in 1985 and was reviewed and accepted by the Board in its RH-2-87 Reasons for Decision.

Solex has received provincial approval to expand the existing NGL plant to $20.4 \times 10^6 \text{ m}^3/\text{d}$ (720 MMcfd). Novagas Canada Ltd. ("NCL") proposes the construction of a gas liquids extraction plant at Taylor, B.C. which would have processing capability of $9.9 \times 10^6 \text{ m}^3/\text{d}$ (350 MMcfd). With respect to make-up volumes associated with the Solex expansion and the NCL plant, Westcoast proposes to charge a toll for transmission on Zones 3 and 4.

1.2 Application

On 12 May 1997, NCL filed an application, on its own behalf and that of certain shippers, requesting that the Board inquire into and determine the appropriateness of certain actions of Westcoast and several provisions of its pipeline Tariff, including its toll schedules. In its application, NCL raised the following issues:

1. Westcoast's right, if any, to cause gas to be diverted from its NEB-regulated system into a privately-owned, non-regulated gas stripping plant owned by Solex, when Westcoast is not the owner of the gas in question and the owners of some of the gas wish to enter into alternative arrangements.
2. Westcoast's right to require that some, but not all, volumes of make-up gas pay a toll on the Westcoast system such that unjust discrimination will occur.
3. The right, if any, of Westcoast and others to carry out such operations by virtue of a Gas Stripping Agreement which is confidential between the parties and not open to public inspection.

NCL requested, among other things, that the Board:

1. To the extent necessary, inquire into this matter further as provided for by section 12 of the Act;
2. Make the necessary orders, pursuant to section 59 of the Act, prohibiting Westcoast from diverting gas, except in accordance with the nominations and directions of shippers; and
3. Order Westcoast to treat all make-up gas transported on Zones 3 and 4 of its system in an equal and non-discriminatory fashion and specifically prohibit the grandfathering of the existing Solex volumes as more particularly described in its application.

On 31 July 1997, the Board issued Hearing Order MH-2-97 which set down NCL's application for a hearing commencing on 15 September 1997 and established the Directions on Procedure and List of Issues.

On 5 August 1997, Westcoast requested a one-week extension to the deadline for filing evidence in the MH-2-97 proceeding. On 8 August 1997, the Board granted Westcoast's request and issued Order AO-1-MH-2-97.

The Board heard evidence in Calgary, Alberta from 15 to 17 September 1997 and final argument on 29 September 1997.

Chapter 2

Views of the Board

The Board was asked by NCL in this hearing to inquire into the matter of the authority of Westcoast to divert its gas stream to the Solex Plant for the purposes of recovering NGL from the gas. The Board's authority to inquire into matters of this nature arises from subsection 12(1) of the Act which provides:

12. (1) The Board has full and exclusive jurisdiction to inquire into, hear and determine any matter
 - (a) where it appears to the Board that any person has failed to do any act, matter or thing required to be done by this Act or by any regulation, certificate, licence or permit, or any order or direction made by the Board, or that any person has done or is doing any act, matter or thing contrary to or in contravention of this Act, or any such regulation, certificate, licence, permit, order or direction; or
 - (b) where it appears to the Board that the circumstances may require the Board, in the public interest, to make any order or give any direction, leave, sanction or approval that by law it is authorized to make or give, or with respect to any matter, act or thing that by this Act or any such regulation, certificate, licence, permit, order or direction is prohibited, sanctioned or required to be done.

After seeking the views of interested parties as to the nature of the issues the Board ought to consider in this hearing, the Board identified, but did not limit itself to, the following issues in the Hearing Order:

1. Whether Westcoast's Tariff allows it to divert gas to Solex for liquids extraction under the gas stripping agreement.
2. Whether amendments to Westcoast's Tariff are required to address the issue of liquids extraction. If so, what amendments would be required?
3. Whether the transportation of make-up volumes should attract a toll and, if so, who should pay those transportation costs?
4. Whether the current tolling arrangements for make-up gas relating to the existing Solex Plant operations should be grandfathered.

Parties raised a number of matters in evidence and argument that were somewhat outside the scope of these issues. After considering all of the evidence, the Board has determined that it ought not to broaden the issues before it beyond those set out in the Hearing Order. Accordingly, this decision focuses on the issues set out above, each of which will be addressed in turn.

Issue 1: Whether Westcoast's Tariff allows it to divert gas to Solex for liquids extraction under the gas stripping agreement.

In his final argument, counsel for NCL provided a detailed legal analysis of what the obligations and rights of Westcoast and shippers, respectively, would be in a common law bailment relationship. He argued that by allowing Solex to strip NGL from the shippers' gas in accordance with the terms of the GSA, Westcoast violated its obligations as bailee of the shippers' gas. Westcoast's counsel, on the other hand, argued that the common law bailment relationship was overridden by the Westcoast Tariff. He further argued that even if this were not the case, Westcoast's actions would not violate any obligations it might have under a common law bailment relationship.

The Board is of the view that the terms of the Tariff govern the relationship between Westcoast and its shippers and effectively modify or override the common law bailment relationship that may have otherwise existed. It is clear that persons have the right in law to alter the common law bailment relationship by way of contract. The Board therefore considers that the obligations of Westcoast should be determined by reference to the Tariff and that, accordingly, it is not necessary to make a determination on what shippers' rights and Westcoast's obligations would be under a common law bailment relationship.

After carefully considering the relevant terms of the Westcoast Tariff, the Board has concluded that the Tariff does not preclude Westcoast from diverting the gas to the Solex Plant in accordance with the GSA entered into by Westcoast and Solex. In reaching this conclusion, the Board had regard to the obligations of Westcoast under Article 4.06 of the Tariff to deliver back to the shipper at the receipt point, not the specific gas that the shipper injected into the system, but a volume of gas which is thermally equivalent to the volume which Westcoast is contracted to deliver. The Board also considered Articles 16.01 and 16.02 in reaching this determination. Those articles provide:

- 16.01 Subject to Section 16.02, Westcoast shall be deemed to be in possession of and control of, and responsible for, all gas received by it at the Receipt Point until such gas is delivered by it at the Delivery Point as if it were the owner thereof and shall have the right at all times to commingle such gas with other gas in the Pipeline System.
- 16.02 Shipper shall be entitled to the quantities of sulphur and Liquid Products recovered by Westcoast from Shippers' gas in the Processing Plants.¹

In view of the wording of these provisions of the Tariff, as well as Article 4.06, the Board is of the view that it is a reasonable interpretation of the Tariff that Westcoast has had authority to divert the gas stream to Solex in accordance with the provisions of the GSA.

¹ "Processing Plants" is a defined term in the Tariff. The definition lists a number of Westcoast processing plants, including the McMahon plant.

Issue 2: Whether amendments to Westcoast's Tariff are required to address the issue of liquids extraction. If so, what amendments would be required?

NCL requested in its application that the Board make the necessary orders pursuant to section 59¹ of the Act, prohibiting Westcoast from diverting gas except in accordance with the nominations and directions of its shippers. This issue raises two principal considerations. The first relates to the right of shippers to the NGL entrained in their gas. The second consideration is whether shippers with gas passing through the McMahon Plant should have the right to require Westcoast to divert their gas to the straddle plant of their choice.

(i) Right of Shippers to their NGL

The role of pipeline companies and the operation of markets have evolved considerably since the implementation of Westcoast's present Tariff provisions. The Board is of the view that, while Westcoast may have been permitted under its present Tariff to divert the gas to the Solex Plant for stripping of the NGL, it should not be allowed to continue to do so. Clearly, the taking of NGL from the gas stream without compensation being paid to the shippers results in serious inequities to shippers who move their gas on this part of the Westcoast system. Indeed, Westcoast acknowledged in the hearing that its proposed enhanced liquids recovery initiative recognizes the rights of shippers to the NGL extracted from their gas. Westcoast further conceded that Tariff changes are required to reflect the right of shippers to the NGL.

The Board is therefore of the view that amendments to the Tariff are required to recognize that shippers are entitled to the NGL entrained in their gas.

(ii) Diversion of Gas

The Board notes that it is the position of Westcoast and Solex that having two straddle plants accessing the gas stream at the McMahon outlet may result in significant extra costs and an unwarranted duplication of facilities. The Board also recognizes, however, that those who ship their gas on Westcoast system through the McMahon plant should be entitled to make business decisions regarding whether Solex or NCL strips the NGL from their gas. It may be that it is ultimately determined that there is a better solution to this issue than having two straddle plants process the residue gas stream at the outlet of the McMahon Plant. The Board considers that it is the market which should ultimately decide this matter. However, in order for the best solution to be advanced, the market must be permitted to operate. The Board views competition as the best means of ensuring that any single player or small group of players do not exercise an undue influence on the market. An important element of competition and market-based solutions in the context of this hearing is the extent to which shippers can exercise the choice to have access to alternative means of getting their products to market. The Board is of the view that the Westcoast shippers ought to have the opportunity to make the choice of whether Solex or NCL will strip the NGL from their gas stream.

With this in mind, the Board directs Westcoast to engage in consultations with its shippers, through the Tolls and Tariff Task Force, to determine what specific amendments should be included in the

¹ Section 59 of the Act provides: The Board may make orders with respect to all matters relating to traffic, tolls or tariffs.

Westcoast Tariff in order to enable shippers to obtain the rights to the liquids entrained in their gas and to permit shippers, should the NCL plant be built, to direct Westcoast to divert their gas to the NCL facility.

In drafting the amendments to the Tariff, Westcoast shall bear in mind the following principles:

- (a) the Tariff must recognize that shippers are entitled to the NGL in their gas streams;
- (b) the Tariff should continue to reflect residue gas quality requirements at any point of injection downstream of the McMahon Plant; and
- (c) Westcoast will retain control of the gas stream exiting the McMahon Plant except to the extent that a shipper with a contract for the extraction of NGL may direct Westcoast to divert its gas to the straddle plant indicated by the shipper.

The Board encourages Westcoast to continue to develop its Liquids Measurement and Allocation ("LMA") system in order to facilitate an equitable allocation of NGL to shippers and, if appropriate, to include provisions respecting the LMA system in the Tariff at the same time as the other amendments are being considered.

Issue 3: Whether the transportation of make-up volumes should attract a toll and, if so, who should pay those transportation costs?

Section 62 of the Act provides:

62. All tolls shall be just and reasonable, and shall always, under substantially similar circumstances and conditions with respect to all traffic of the same description carried over the same route, be charged equally to all persons at the same rate.

Currently, Solex provides make-up volumes of gas in exchange for the NGL that have been extracted from the gas to ensure that Westcoast can meet its Tariff requirements for heating content of the gas at the delivery point. These make-up volumes do not attract a toll under the present arrangement with Westcoast. NCL has argued that, should this so-called "phantom toll" continue and be grandfathered following an expansion of the Solex plant, it would result in a situation of unjust discrimination by Westcoast in its treatment of Solex and NCL. This would be so because Westcoast has indicated that NCL would be required to pay a toll for all of its make-up volumes.

Currently only the Solex plant is operating downstream of the McMahon Plant so this particular issue is to some extent prematurely before the Board. However, at this point, the Board's view is that, if there were two straddle plants downstream of the McMahon Plant, and one was required to pay a toll for make-up volumes while the other was not, this would likely result in unjust discrimination contrary to section 62 of the Act. Accordingly, the Board would expect that the volumes coming out of each of the NCL and Solex plants would be treated equally by Westcoast in terms of tolls.

Issue 4: Whether the current tolling arrangements for make-up gas relating to the existing Solex Plant operations should be grandfathered.

In view of the determination of the Board in respect of Issue 3, it is not necessary to address this issue further.

Chapter 3

Disposition

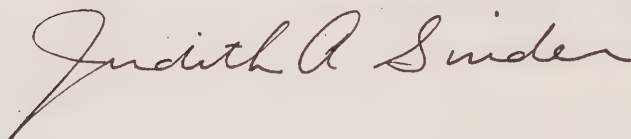
The foregoing together with Order MO-17-97 constitutes our Decision and Reasons for Decision on this matter.



A. Côté-Verhaaf
Presiding Member



K.W. Vollman
Member



J.A. Snider
Member

Calgary, Alberta
October 1997

Appendix I

Order MO-17-97

IN THE MATTER OF sections 12, 59, 62 and all other relevant sections of the *National Energy Board Act*; and

IN THE MATTER OF an application by Novagas Canada Ltd. ("NCL") dated 12 May 1997 requesting that the Board inquire into the practices of Westcoast Energy Inc. ("Westcoast") with respect to gas stripping arrangements at Taylor, British Columbia.

BEFORE the Board on 6 October 1997.

WHEREAS NCL filed an application dated 12 May 1997 requesting that the Board inquire into and determine the appropriateness of certain actions of Westcoast respect to gas stripping arrangements at Taylor, British Columbia;

AND WHEREAS the Board has examined the application at an oral hearing held in Calgary, Alberta;

AND WHEREAS the Board has determined that amendments are required to Westcoast's Tariff to enable shippers to obtain the rights to the natural gas liquids entrained in their gas and to permit shippers, should the NCL plant be built, to direct Westcoast to divert their gas to the NCL facility;

IT IS ORDERED THAT:

1. Westcoast shall enter into consultations with shippers to determine what Tariff amendments are required to carry this decision into effect and report back to the Board with the proposed amendments, for approval by the Board, within 90 days of the release of this Decision.

NATIONAL ENERGY BOARD

M. L. Mantha
Secretary

